

INDIANA DEPARTMENT OF STATE REVENUE

RULING #2000-02 IT

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ISSUE

Gross Income Tax, Adjusted Gross Income Tax and Supplemental Net Income Tax – Eligibility for Consolidated Filing for Gross Income Tax, Adjusted Gross Income Tax and Supplemental Net Income

Authority: IC 6-2.1-5-5, IC 6-2.1-4-6, IC 6-3-1-11, IC 6-2.1-3-25, Rule 45 IAC 1.1-3-12, Rule 45 IAC 1.1-1-3, Rule 45 IAC 1.1-2-13, IC 6-2.1-2-2, Rule 45 IAC 1.1-2-13, IC 6-3-8-2, IRC Section 63, IC 6-3-2-2, Rule 45 IAC 3.1-1-153, IC 6-3-2-2.2, IC 6-3-4-14, Internal Revenue Regulation Section 301.7701(1-3), IRC Sections 7701(a)(3) & (a)(7)

The taxpayer requests the Department to rule on the eligibility for consolidated filing for Gross Income Tax, Adjusted Gross Income Tax and Supplemental Net Income Tax for a proposed business structure.

STATEMENT OF FACTS

The taxpayer files a consolidated federal income tax return, including income from more than forty separately organized subsidiary corporations, limited liability companies and corporate partnerships. Each business entity is organized separately for business purposes unrelated to tax considerations. The product lines and management practices of this client are such that the businesses of this group of companies do not satisfy the tests to qualify as one unitary business. However, there is a unitary relationship between some specific companies within the group. These corporations, limited liability companies and partnerships are organized under the laws of various states. Most have no business activities in the State of Indiana, and are not registered with the Secretary of State in Indiana. Some partnerships and limited liability companies are owned by members of the client's group of companies and unrelated companies outside the group. Others are partnerships between members of the taxpayer's organizational structure.

The proposed subgroup of companies is made up of the taxpayer, four subsidiary corporations, two limited liability companies and two partnerships. Each company is further described below:

The Taxpayer – The taxpayer is registered with the Indiana Secretary of State as a corporation, qualified to conduct business in Indiana. Its commercial domicile is outside the State of Indiana. All tangible property is located outside the State of Indiana but this company has one employee working in the State of Indiana. The employee works at below referenced Company G's Indiana business location providing operational services to Company G on a daily basis. The taxpayer's only Indiana income is income from Company B, Company C, Company E, Company H and Company K described below. The taxpayer also owns interest in other partnerships, limited liability companies, and corporations that do not conduct any business in Indiana. The taxpayer has substantial investment in each of the companies that it holds an interest in such that any losses passed up from flow-through entities are deductible for federal income tax purposes.

Company B. B is registered with the Indiana Secretary of State as a corporation qualified to conduct business in Indiana. B's commercial domicile is outside the State of Indiana. All of B's tangible property and employees are located outside the State of Indiana. B's only Indiana income is dividend income from Company C, further described below. Company B has substantial investment in each of the companies that it holds an interest in such that any losses passed up from flow-through entities are deductible for federal income tax purposes.

Company C. C is registered with the Indiana Secretary of State as a limited liability company, qualified to conduct business in Indiana, and is treated as a partnership for federal income tax purposes. C is owned entirely by the taxpayer and Company B. Company C, Company B and the taxpayer do not share a "unitary relationship". C's commercial domicile is outside the State of Indiana. All of C's tangible property and employees are outside the State of Indiana. C's only Indiana income is dividend income from Company D, further described below. Company C has substantial investment in Company D such that any loss by Company D would be deductible for federal income tax purposes.

Company D. D is a limited partnership between Company C and an unrelated corporation. The percentage each partner owns varies from time to time within a tax year. However, at no time does either partner own 80% or more of the partnership. D is not a publicly traded

partnership that is treated as a corporation under section 7704 of the Internal Revenue Code. D manufactures and sells tangible personal property at an Indiana business location. In any given year, D may have a net loss or profit for federal income tax purposes.

Company E. E is registered with the Indiana Secretary of State as a corporation qualified to conduct business in Indiana. E's commercial domicile is outside the State of Indiana. All of E's tangible property and employees are located outside the State of Indiana. E's only Indiana income is income from Company F and Company G, further described below. Company E has substantial investment in each of the companies that it holds an interest in such that any losses passed up from flow-through entities are deductible for federal income tax purposes.

Company F. F is registered with the Indiana Secretary of State as a corporation qualified to conduct business in Indiana. F's commercial domicile is outside the State of Indiana. All of F's tangible property and employees are located outside the State of Indiana. F's only Indiana income is income from Company G, further described below. Company F has substantial investment in Company G such that any loss by Company G would be deductible for federal income tax purposes.

Company G. G is registered with the Indiana Secretary of State as a limited liability company, qualified to conduct business in Indiana, and is treated as a partnership for federal income tax purposes. G is owned entirely by Company E and Company F. Company G, Company F and Company E do not share a "unitary relationship". G manufactures and sells tangible personal property at an Indiana business location. In any given year, G may have a net loss or profit for federal income tax purposes.

Company H. H is registered with the Indiana Secretary of State as a corporation qualified to conduct business in Indiana. E's commercial domicile is outside the State of Indiana. All of H's tangible property and employees are located outside the State of Indiana. H's only Indiana income is income from Company K, further described below.

Company K. K is a limited partnership, owned entirely by the taxpayer (limited partner) and Company H (general partner). The taxpayer does not participate in control of the business of Company K. Under the Federal "check the box" regulations, K has elected to be treated as association, and is taxed as a corporation. K manufactures and

sells tangible personal property at an Indiana business location. In most years, K is expected to have a net income for federal and state tax purposes.

No other companies in the taxpayer's organizational structure have income from Indiana sources or a certificate of authority to transact business in Indiana.

DISCUSSION

IC 6-2.1-5-5 provides that for gross income taxation corporations are affiliated if at least eighty percent (80%) of the voting stock of one (1) corporation (exclusive of directors' qualifying shares) is owned by the other corporation. Every corporation affiliated with another corporation is affiliated with every corporation that is affiliated with such other corporation. All corporations so affiliated constitute an affiliated group.

Corporate members of an affiliated group that are incorporated in the State of Indiana or are authorized to do business in the State of Indiana may file a consolidated gross income tax return.

Here, the taxpayer, Company B, Company E, Company F and Company H are defined as an affiliated group and are eligible to file a consolidated Indiana gross income tax return. Pursuant to IC 6-2.1-4-6, an affiliated group of corporations filing consolidated return, as provided by IC 6-2.1-5-5, is entitled to a deduction from the gross income reported on such a return. The amount of the deduction equals the total amount of gross income received during the taxable year from transactions between members of the group that are incorporated or authorized to do business in Indiana.

Company K, although treated as a corporation for adjusted gross income taxation (IC 6-3.1-11) is treated as a limited partnership for gross income taxation, pursuant to IC 6-2.1-3-25 and Rule 45 IAC 1.1-3-12, therefore, is not eligible to participate in an Indiana consolidated gross income tax return.

The taxpayer's distributive share from Company K is not subject to gross income tax, pursuant to Rule 45 IAC 1.1-1-3(b)(7), as the taxpayer is a limited partner and does not participate in the control of the business. The taxpayer's distributive share from Company C (treated as a partnership for gross income taxation pursuant to Tax Policy Directive #2) is subject to gross income tax as stated by Rule 45 IAC 1.1-2-13. Any income received from Company G by the taxpayer for services provided by the taxpayer's employee to Company G is, also, subject to gross income tax as provided by Rule 45 IAC 1.1-1-3(b)(2) and IC 6-2.1-2-2.

Company B's distributive share from Company C (treated as a partnership for gross income taxation) and Company F's and Company E's distributive shares from Company G (treated as a partnership for gross income taxation) are subject to gross income tax pursuant to Rule 45 IAC 1.1-2-13. Company H's distributive share from Company K

(treated as a limited partnership for gross income taxation) is subject to gross income tax, pursuant to Rule 45 IAC 1.1-2-13, as Company H is a general partner.

For adjusted gross income taxation and supplemental net income taxation (note that all determinations applicable to adjusted gross income tax are, also, applicable to supplemental net income tax as provided by IC 6-3-8-2) the taxpayer, by virtue of having an employee providing services to Company G in Indiana, is defined as deriving adjusted gross income from Indiana, therefore, its Internal Revenue Code Section 63 "taxable income" with modifications, if any, is subject to apportionment as stated by IC 6-3-2-2. The taxpayer's distributive share from Company C [treated as a partnership for adjusted gross income taxation (IC 6-3-11)] is subject to adjusted gross income tax pursuant to Rule 45 IAC 3.1-1-153. The taxpayer's distributive share from Company K [treated as a corporation for adjusted gross income taxation (IC 6-3-1-11)] is not subject to adjusted gross income tax, pursuant to IC 6-3-2-2 and IC 6-3-2-2.2, as the distributive share is treated as a dividend to the taxpayer and the taxpayer's commercial domicile is outside Indiana.

Company B's distributive share from Company C [treated as a partnership for adjusted gross income taxation (IC 6-3-1-11)] and Company F's and Company E's distributive shares from Company G [treated as a partnership for adjusted gross income taxation (IC 6-3-1-11)] are subject to adjusted gross income tax pursuant to Rule 45 IAC 3.1-1-153. Company H's distributive share from Company K [treated as a corporation for adjusted gross income taxation (IC 6-3-1-11)] is not subject to adjusted gross income tax, pursuant to IC 6-3-2-2 and IC 6-3-2-2.2, as the distributive share is treated as a dividend to Company H and Company H's commercial domicile is outside Indiana.

IC 6-3-4-14 provides that an affiliated group of corporations shall have the privilege of making a consolidated adjusted gross income tax return. The term "affiliated group" means an "affiliated group" as defined in Section 1504 of the Internal Revenue Code with the exception that the affiliated group shall not include any corporation which does not have adjusted gross income derived from sources within the State of Indiana. Internal Revenue Section 1504 states that "affiliated group" means;

(a)(1)(A)-1 or more chains of includible corporations connected through stock ownership with a common parent corporation which is an includible corporation, but only if –

(B)(i) the common parent owns directly stock meeting the requirements of paragraph (2) in at least 1 of the other includible corporations, and

(ii) stock meeting the requirement of paragraph (2) in each of the includible corporations (except the common parent) is owned directly by 1 or more of the other includible corporations.

(2) 80-percent voting and value test. – The ownership of stock of any corporation meets the requirement of this paragraph if it -

- (A) possesses at least 80 percent of the total voting power of the stock of such corporation, and
- (B) has a value equal to at least 80 percent of the total value of the stock of such corporation.

The taxpayer, Company B, Company E, Company F and Company H all are part of an "affiliated group" as defined by Internal Revenue Code Section 1504. Company K, electing to be treated as an association and taxed as a corporation [Internal Revenue Regulation Section 301.7701-(1-3)], also, is part of an Internal Revenue Code Section 1504 "affiliated group" as the term "corporation" includes associations and the term "stock" includes shares in associations pursuant to Internal Code Sections 7701(a)(3) and (a)(7).

As mentioned previously, in addition to being defined as a member of an "affiliated group" all participants in a consolidated adjusted gross income tax return must have "adjusted gross income derived from sources within Indiana". IC 6-3-2-2(a) defines adjusted gross income derived from sources within Indiana. The taxpayer, Company B, Company E, Company F and Company K all have "adjusted gross income derived from sources within Indian", therefore, are eligible to participate in and Indiana consolidated adjusted gross income tax return. Company H, although part of the taxpayer's "affiliated group", does not have adjusted gross income derived from Indiana, hence, is not eligible to participate in an Indiana consolidated adjusted gross income tax return.

RULING

The Department rules that for Indiana gross income taxation the taxpayer, Company B, Company E, Company F and Company H are eligible to participate in a consolidated gross income tax return. Company K is not eligible to participate.

The taxpayer, Company B, Company E, Company F and Company K are eligible to participate in a consolidated adjusted gross income tax return. Company H is not eligible to participate.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein, are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this

ruling, a change in a statute, a regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

Department of State Revenue